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CHARLES ELMORE

IN THE

Supreme Court of the United States

OCTOBER TERM, A. D. 1934.

In The Matter of
THE CHICAGO, ROCK ISLAND & PACIFIC RAILWAY COMPANY, Debtor.

Nos. 479 480

CONTINENTAL ILLINOIS NATIONAL BANK AND TRUST COMPANY OF CHICAGO, Petitioner, *vs.* THE CHICAGO, ROCK ISLAND & PACIFIC RAILWAY COMPANY, ET AL., Respondents.

Nos. 481 482

THE CHASE NATIONAL BANK OF THE CITY OF NEW YORK, Petitioner, *vs.* THE CHICAGO, ROCK ISLAND & PACIFIC RAILWAY COMPANY, ET AL., Respondents.

Nos. 483 484

MISSISSIPPI VALLEY TRUST COMPANY, Petitioner, *vs.* THE CHICAGO, ROCK ISLAND & PACIFIC RAILWAY COMPANY, ET AL., Respondents.

Nos. 485 486

HARRIS TRUST AND SAVINGS BANK, Petitioner, *vs.* THE CHICAGO, ROCK ISLAND & PACIFIC RAILWAY COMPANY, ET AL., Respondents.

Nos. 487 488

THE NEW YORK TRUST COMPANY, Petitioner, *vs.* THE CHICAGO, ROCK ISLAND & PACIFIC RAILWAY COMPANY, ET AL., Respondents.

PETITION FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT, AND BRIEF IN SUPPORT THEREOF.

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PETITION FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT, AND BRIEF IN SUPPORT THEREOF.

The above named petitioners, by the undersigned, their attorneys, respectfully pray that writs of certiorari issue to review the judgments of the Circuit Court of Appeals for the Seventh Circuit, entered on

July 23, 1934 (R. 327-31, 333-7), affirming an injunctional order of the District Court for the Northern District of Illinois, Eastern Division, entered on November 22, 1933. (R. 101-104).

PRINCIPAL QUESTIONS PRESENTED.

I. Has a district court, sitting in bankruptcy in a proceeding for the reorganization of a railroad under Section 77 of the Bankruptcy Act, power (contrary to the rule laid down by this Court in ordinary bankruptcy proceedings) summarily to enjoin the sale by a pledgee of validly pledged collateral, consisting of mortgage bonds of the pledgor railroad and of a subsidiary, when such sale is authorized by the pledge agreement and does not require judicial proceedings.

II. Whether, in such a proceeding, a district court sitting in one district may enjoin the sale of such collateral held by a bank which (a) is not a party to the proceeding, (b) is not a resident of or present within such district and (c) holds the collateral outside such district.

III. Does Section 77, as construed by the court below, violate the Fifth Amendment by impairing preexisting contract rights of petitioners (the pledgees) to sell the pledged collateral at any time permitted by the pledge agreement.

STATUTES INVOLVED.

The pertinent provisions of Section 77, Chapter VIII, of the Bankruptcy Act (Act of March 3, 1933, c. 204, 47 Stat. 1474; U. S. C. A., Title 11, Sec. 205) and other relevant statutes appear in the Appendix, pp. 29-33, *infra*.

STATEMENT.

On November 22, 1933, in a railroad reorganization proceeding under Section 77 of the Bankruptcy Act, entitled "In the Matter of The Chicago Rock Island and Pacific Railway Company, Debtor," (said railroad being herein referred to as "Debtor"), the District Court entered an order enjoining these petitioners and Reconstruction Finance Corporation (herein referred to as "R. F. C.") from selling collateral held by each of them as security for promissory notes of said Debtor, until further order of the court. (R. 101-104).

Three of the petitioners (The Chase National Bank of the City of New York, The New York Trust Company and Mississippi Valley Trust Company, referred to herein as the "nonresident banks"), unlike R. F. C. and the other two petitioners (Continental Illinois National Bank and Trust Company of Chicago and Harris Trust and Savings Bank, referred to herein as the "Chicago banks"), were not and are not residents of or doing business in the Northern District of Illinois. (R. 116-119). Neither any of the petitioners nor R. F. C. were made parties to the proceeding, nor were any thereof ever served with process. The only notice, received by any of them, of the petition (pursuant to which the injunction was issued) was by registered mail. (R. 55-56).

In response to such notice by mail, the nonresident banks, the Chicago banks and the R. F. C. appeared specially to object to the jurisdiction of the court over them (R. 68, 70, 71, 72, 73, 75). The R. F. C. and the Chicago banks also objected to the jurisdiction of the court (a) over the subject matter, and

(b) to grant the injunction in a summary proceeding. (R. 70, 71, 72, 75).

In order to obviate the question whether the proceeding in the trial court was a "controversy" or a "proceeding" in bankruptcy, each petitioner and R. F. C. took two separate appeals from the injunctional order,—one of which was allowed by the trial court and the other by the Circuit Court of Appeals. (R. 124, 133, 140, 148, 155, 163, 215, 229, 242, 254, 266, 278.) The two appeals of each defendant were consolidated for hearing in the Circuit Court of Appeals. (R. 287-298). None of the appeals was dismissed and on July 23, 1934 that court affirmed the injunctional order (R. 313-326) and entered twelve judgments accordingly. (R. 327-338).

This petition is filed jointly by all appellants below except R. F. C. A separate petition for writs of certiorari to review the judgments of the Circuit Court of Appeals is being filed by R. F. C.

The injunctional order was entered upon the following record:

On June 7, 1933 the Debtor filed in the District Court its original petition, alleging that it was "unable to meet its debts as they mature," and that it desired to effect a plan of reorganization under Section 77 of the Bankruptcy Act. (R. 2-5). On the same day the court entered an order approving the petition as properly filed, and directing the Debtor, pending further order, to operate its railroads, subject to supervision of the court. (R. 6-10). Thereafter, the Debtor conducted its business pursuant to said order until November 22, 1933, on which date the court appointed

trustees of the Debtor's property. (R. 105-107). By orders entered August 28, 1933 and October 24, 1933, petitions of certain of the Debtor's subsidiaries to effect plans of reorganization under said Section 77 in connection with, or as a part of, the plan of reorganization of the Debtor were approved by the District Court. (R. 26-28, 97-99).

On September 26, 1933, prior to the appointment of trustees, the Debtor filed in the District Court a petition (R. 37-43) which alleged, in substance, that it was indebted to R. F. C. in the sum of $13,659,877.58 evidenced by six notes, dated on or prior to April 1, 1933 and due March 1, 1934; that said notes were secured by pledge to R. F. C. of collateral, described in detail, consisting chiefly of mortgage bonds of the Debtor and of its subsidiaries aggregating approximately $40,000,000 in principal amount; and that all interest on said notes had been paid to the date of the petition, the next installment being due October 1, 1933. The petition further alleged that the Debtor was also indebted to these petitioners in the total face amount of $3,866,923.34 (after application of deposits by two of petitioners), evidenced by notes payable to the respective petitioners, dated August 1, 1932 and due March 1, 1934, and secured by pledge to each of petitioners of mortgage bonds of the Debtor and of one of its subsidiaries in the aggregate face amount of $14,409,000. (R. 39-40).

From exhibits attached to said Debtor's petition (R. 52-55) it appears that each of the notes held by the petitioners provides that it shall become due in case of, among other events, (1) nonpayment of interest, (2) the insolvency of the Debtor, (3) the appointment of a receiver for the Debtor, or (4) nonpayment of in-

terest on any of said notes of the Debtor held by R. F. C. (R. 53); and each note provides that (R. 54):

> "Upon default of any kind hereunder, the payee may sell in * * * New York City, or elsewhere, * * * all or any of the security held for the payment of this note, at any broker's board or at public or private sale, without * * *. notice * * * and the payee may be the purchaser of any or all property, rights and/or interests so sold * * *."

The Debtor's petition alleged further that the value of the collateral securing each of said notes was substantially in excess of the amount of said note; that if the holders of the notes should sell said collateral it would cause a substantial and irreparable loss to the trust estate; and that a forced sale thereof "at the present time * * * *might* result" (Italics ours) in a substantial deficiency judgment against the Debtor, and would dilute the respective interests in the trust estate of the holders of the Debtor's bonds, of other creditors of the trust estate, and of the Debtor itself. (R. 40-41). The petition asked for instructions of the court as to the payment of interest due R. F. C. on October 1, 1933 (September 30, 1933), and also that the court determine (R. 43):

> "* * * whether the Court should enjoin and restrain the holders of the said collateral notes, *in the event of default in the payment of interest thereon,* or other default therein, from selling and converting the said collateral, or any part thereof." (Italics ours).

In support of their respective special appearances the nonresident banks filed affidavits which disclosed that they were not residents of or present within the Northern District of Illinois, were not parties to the proceeding, and had never been served with process therein. (R. 116-119).

A Protective Committee for the Debtor's First and

Refunding Mortgage Bonds appeared and filed the affidavit of its Chairman, Dwight S. Beebe (R. 113-115), which alleged that approximately $145,749,050 face amount of bonds and stock of the Debtor's System were pledged with Trustees of three of the Debtor's mortgages; "that in certain events described in the Indentures under which the aforesaid Trustees are acting, such Trustees are given the right to sell such collateral"; that a decision that the R. F. C. and the banks should not be enjoined from selling the collateral held by them "would also determine that the Trustees under the three bond issues mentioned above had the right to sell the $145,749,050 total face amount of capital obligations of the System pledged with them"; and that the "*position of this Committee* * * * is that the interests of the bondholders * * * and of the Debtor's estate generally would best be served * * * by a decision requiring all holders of secured claims to retain their collateral until a plan of reorganization is prepared, approved and put into effect." (Italics ours)

Thereupon, on the same day (September 26, 1933), the court authorized the Debtor to pay interest due R. F. C. on September 30, 1933, but reserved decision on the matter of the injunction. (R. 75-77).

Thereafter, on November 22, 1933, the District Court entered an order restraining these petitioners and R. F. C. from selling or disposing of the collateral held by them, or any part thereof, until further order of the court. (R. 101-104). This order was entered by the trial judge without any opinion, written or oral, and *solely upon said petition of the Debtor, the Beebe affidavit, and the affidavits filed by the nonresident banks,* which latter affidavits merely questioned the court's jurisdiction. From the recitals in the order, it appears that the judge based it on the ground that a sale of the collateral would interfere with a reorganization and

that therefore the court had ample power to enjoin the sale. (R. 103-104).

Upon the appeals from this injunctional order the Circuit Court of Appeals held:

1. That the injunction was an exercise of authority which was necessary to the effective use of the powers conferred upon the District Court by Section 77. (R. 324).[1]

2. That the jurisdiction of the District Court under Section 77 is "coextensive with the territorial boundaries of the United States," and therefore the injunction was lawful notwithstanding the fact that the nonresident banks, and the collateral held by them, were not within the Northern District of Illinois. (R. 322).

3. That the injunction merely restrained the "pursuit of a remedy" by those enjoined, and therefore (a) could be issued in a summary proceeding, and (b) did not violate the Constitution of the United States. (R. 324).

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1. Two misapprehensions of fact, which seem strongly to have influenced the Circuit Court of Appeals in affirming the injunctional order, should be noted:

(a) The court stated (R. 325) that

> "Appellants have received and will probably continue to receive the prompt payment of interest upon their claims secured by the debtor's and its subsidiaries' bonds."

Although interest was paid, as due, upon the Debtor's notes held by the banks and R. F. C. until the injunction, *no interest whatever, due thereafter, has been paid.* (R. 341-342). The notes held by petitioners and R. F. C. matured on March 1, 1934 (R. 38-39), and the principal thereof has not been paid.

(b) The court also stated (R. 325) that the District Court—

> "sought to protect the great mass of debtor's creditors *without injuring the position of appellants* • • •." (Italics ours.)

The fact is that when the Debtor's petition for an injunction was filed, the collateral held by these petitioners as security for notes of the Debtor had a market value (based on last prior sales on the New York Stock Exchange) of $4,269,000, which was in excess of the amount of the indebtedness ($3,866,923.34) then owing to petitioners. At the time of the writing of this petition (October 15, 1934), the market value of said collateral (on the same basis) is $2,614,755. These figures indicate that already the injunction has damaged the petitioners in excess of $1,250,000.

REASONS FOR GRANTING THE WRITS.

I.

The Decision of the Circuit Court of Appeals—That a District Court, in a Railroad Reorganization Proceeding Under Section 77 of the Bankruptcy Act, Has Power to Enjoin a Pledgee from Selling, in Accordance with the Contract of Pledge, Mortgage Bonds Issued by the Railroad or Its Subsidiaries and Validly Pledged by the Railroad to Secure Its Debt—Asserts a Power Which This Court Has Held Does Not Exist in an Ordinary Bankruptcy Proceeding and Raises a Question of Far Reaching Importance Which Should Be Settled by This Court.

A. Since the decision of this Court in *Jerome* v. *McCarter,* 94 U. S. 734, 739 (1876), it has been settled law that a bankruptcy court is without authority to enjoin the sale of collateral validly pledged by the bankrupt to, and in the possession of, the pledgee, even though the collateral consists of mortgage obligations of the bankrupt of a par value in excess of the amount of the loan. See *In re Ironclad Mfg. Co.,* 192 Fed. 318 (C. C. A. 2nd, 1912); *Worth* v. *Marshall Field & Co.,* 240 Fed. 395, 397 (C. C. A. 4th, 1917); *Turner* v. *Metropolitan Trust Co.,* 207 Fed. 495, 499-500 (C. C. A. 9th, 1913). The decision below overturns this well settled rule as applied to railroad reorganization proceedings.

B. The decision will affect a large number of similar cases and, consequently, a large amount of collateral loans.

There are now pending 12 proceedings under Section 77 for the reorganization of interstate railroad systems.[2] The actual number of railroads involved is con-

2. According to a recent letter from the Director of the Bureau of Finance of the Interstate Commerce Commission, dated October 3, 1934.

siderably larger since, as in the instant case, the bankruptcy of the parent corporation usually results in the filing of petitions by all its subsidiaries.[3]

Moreover, the decision is of even wider application since it may apply not only to railroad reorganizations but also to corporate reorganizations generally. On June 7, 1934, Congress enacted Section 77 B of the Bankruptcy Act (U. S. C. A., Title 11, Sec. 207), which, in substance, makes applicable to corporations generally, including public utilities, the bankruptcy reorganization procedure set up by Section 77. Since the jurisdictional provisions of Sections 77 and 77 B are closely identical (see Comparative Table, Appendix, pp. 32-33, *infra*), it would seem that the decision of the court below may be applicable to proceedings under Section 77 B. The number of proceedings already instituted under Section 77 B is large.[4]

C. Literally, hundreds of millions of dollars of now outstanding collateral loans to railroads and other corporations—which must have been made, in part, in reliance upon the rule of law laid down in *Jerome* v. *McCarter*, 94 U. S. 734, *supra*, and numerous other later decisions—are seriously affected by the decision of the Circuit Court of Appeals.

Even if the decision be regarded as applicable only to collateral loans (a) to railroads (b) where the collateral consists of secured obligations of the railroad,

3. In the pending application of the Class 1 railroads to the Interstate Commerce Commission for rate increases, testimony was presented to the effect that at the present time twenty-six Class 1 railroads, operating 40,565 miles of track, are in the hands of trustees in bankruptcy or receivers. (See New York Herald Tribune, October 2, 1934, p. 23.)

4. A search of the docket of the District Court for the Southern District of New York discloses that in less than five months since the enactment of Section 77 B more than 80 proceedings under that section have been filed in that one district alone.

the aggregate amount of collateral loans affected by the decision is great, since, in recent years, the practice of railroads of pledging their own bonds as security for their own debts has assumed very large proportions. (See Hatch, "A Form of Depression Finance—Corporations Pledging Their Own Bonds," 47 Harv. L. Rev. 1093, 1095). In 1932 alone, the railroads of the United States issued over $1,000,000,000 of mortgage bonds, about 90% of which, it has been estimated, were pledged by the railroads to secure total borrowings of about $650,000,000. (See United States Daily, January 18, 1933, p. 2005; see also Hatch, *ibid,* 47 Harv. L. Rev. 1093, 1095). In one case alone, the Interstate Commerce Commission authorized the New York Central to issue $100,000,000 of its mortgage bonds by way of pledge for the railroad's own debts. (See 180 I. C. C: 155 and 349).

D. The decision may have far reaching effects upon industry and commerce.

Present day borrowings by railroads are primarily for short terms, and loans are chiefly obtained by the use of securities as collateral. In such transactions the borrower is able to secure the requisite funds with despatch by pledge of its securities; the lender is protected by the collateral pledged, and most important of all, his loan is liquid by reason of the right to realize quickly upon the collateral, if necessary. Until this Court has ruled upon the power of a court to enter an injunction under the circumstances involved in the instant case, pledgees, holding millions of dollars face amount of railroad mortgage bonds as collateral security for indebtedness of the railroad corporations issuing such bonds, are and will remain in doubt as to their rights in the event of default in the payment of the indebtedness secured or the institution of reorganization proceedings under

said Section 77, and hence in doubt as to the value of the security held. A further natural—almost inevitable—result of such uncertainty will be that railroads will find it increasingly difficult to make or renew short-time loans, even though adequate collateral security, from the point of view of value, is offered therefor.

II.

The Decision of the Court—That, in a Proceeding Under Section 77, a District Court in One District May Issue an Injunction Against the Sale of Pledged Collateral Held by One Who (a) Is Not a Party to the Proceeding, (b) Is Not Present Within Such District, and (c) Holds Possession of the Pledged Collateral Outside the District —Also Raises Issues of General Importance.

(*This reason is urged only by the nonresident banks.*)

A. Under long established policy "the jurisdiction of a district court *in personam* has been limited to the district of which the defendant is an inhabitant or in which he can be found." See *Robertson* v. *Railroad Labor Board*, 268 U. S. 619, 627 (1925). Whether Congress intended, *in the absence of language to that effect in the statute,* to effect a revolutionary departure from such policy is a question peculiarly within the jurisdiction of this Court.

B. The holding that the jurisdiction of the court in a proceeding under Section 77 is "coextensive with the territorial boundaries of the United States" raises problems in the administration of the statute, because of (a) the absence of any mechanism in Section 77, or elsewhere, for the functioning of a court with nationwide territorial limits, and (b) the lack of any provision authorizing the process of the court to run throughout the United States—a power which is vital if the court is to exercise, *as to the entire nation,* the

many powers conferred upon a bankruptcy court. See Section 2 of the Bankruptcy Act, as amended; U. S. C. A., Title 11, Sec. 11.

C. The decision of the court below imposes new and severe burdens upon many banks and business houses. Much business is conducted with little regard to intervening state or other lines. Business houses in New York, for example, are constantly dealing with railroads all over the country. If a district court may, in a proceeding under Section 77, issue an injunction against a creditor of the debtor *anywhere in the United States*, merely upon notice by mail, all creditors of the debtor must submit themselves to the jurisdiction of that court, although such creditors may be residents of New York and the bankruptcy proceedings may be pending in California, or else must assume the risk of court action adverse to their interests.

III.

This Court Should Determine Whether Section 77, As Construed by the Circuit Court of Appeals, Violates the Fifth Amendment in So Far as It Impairs Petitioners' Pre-existing Contract Rights to Sell the Pledged Collateral, Pursuant to the Terms of Valid Pledge Agreements Made Prior to the Effective Date of Section 77.

The holding of the court that the injunction did not deprive petitioners of a substantial right but merely of a remedy is based upon a premise, the error of which is established by the fact that the market value of the collateral held by these petitioners has actually declined more than $1,600,000 since the filing of the Debtor's petition for an injunction, and petitioners' loans are *now* more than $1,250,000 in excess of the present market value of the collateral and are *now* inadequately secured. (See footnote 1 (b), p. 8, *ante*.)

IV.

The Decision of the Circuit Court of Appeals Is in Conflict with Decisions of This Court Under the Bankruptcy Act. Moreover the Decision of the Court Below Is Not Supported by the Record.

Hiscock v. *Varick Bank of New York*, 206 U. S. 28, 40 (1907);

Jerome v. *McCarter*, 94 U. S. 734, 739 (1876); and

Acme Harvester Co. v. *Beekman Lumber Co.*, 222 U. S. 300, 310 (1911).

See also, *In re Ironclad Mfg. Co.*, 192 Fed. 318 (C. C. A. 2nd, 1912).

WHEREFORE it is respectfully submitted that the writs of certiorari herein prayed should issue.

October, 1934.

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BRIEF IN SUPPORT OF PETITION.

OPINIONS BELOW.

No opinion was rendered by the District Court. The opinion of the Circuit Court of Appeals (R. 313-326) is not yet reported.

JURISDICTION.

The judgments of the Circuit Court of Appeals were entered July 23, 1934. (R. 327-331, 333-337). The jurisdiction of this Court rests upon Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED, STATUTES INVOLVED, ETC.

The questions presented and a statement of the case appear in the petition. The applicable statutes are set forth in the Appendix, pp. 29-31, *infra*.

SPECIFICATION OF ERRORS TO BE URGED.

The Circuit Court of Appeals erred:

1. In holding that, in a proceeding under Section 77 of the Bankruptcy Act, a district court may summarily enjoin the sale (not requiring judicial proceedings) of collateral which has been validily pledged by the debtor as security for a

note of the debtor, when such collateral consists of secured bonds of the debtor and of a subsidiary corporation of a par value substantially in excess of the amount of the note.

2. In holding that, in such a proceeding, a district court sitting in one judicial district may lawfully enjoin the sale of collateral which has been validly pledged as security for a note of the debtor although the pledgee (a) is not a party to the proceeding, (b) is not a resident of or present within such judicial district, and (c) holds the pledged collateral beyond the limits of such district. (*To be urged only by the nonresident banks.*)

3. In holding that a sale of the collateral held by petitioners would hinder and prevent the preparation and consummation of a plan of reorganization of the Debtor.

4. In holding that Section 77 of the Bankruptcy Act, as construed and applied by that court, did not violate the Fifth Amendment of the Constitution as applied to petitioners.

5. In failing to hold that the District Court had no jurisdiction to enter the injunctional order.

ARGUMENT.

I.

Section 77 Does Not, Either Expressly or by Implication, Confer Jurisdiction on a Court of Bankruptcy to Enjoin a Pledgee from Selling Pledged Collateral Upon Default, Pursuant to the Terms of the Pledge Agreement, Even Though the Collateral Consists of Mortgage Bonds of the Debtor.

It has long been established law that, in ordinary bankruptcy proceedings, a pledgee cannot be deprived, in either a summary or a plenary proceeding, of his contract right to sell (at a sale not requiring judicial proceedings) collateral pledged to him by the bankrupt. The rule is the same even though the pledged collateral consists of secured obligations of the bankrupt himself. Section 77 does not, expressly or by implication, purport to change this rule. The "omnibus clause" of the Bankruptcy Act (see Bankruptcy Act, Section 2(15), Appendix, *infra*, page 29), which was in force long before the passage of Section 77, does not confer additional jurisdiction to enter the injunction.

The opinion of the Circuit Court of Appeals expressly avoids a discussion of the applicable decisions prior to the enactment of Section 77 (R. 319-320).

In *Hiscock* v. *Varick Bank of New York*, 206 U. S. 28 (1907), this Court held (p. 40) that, under Section 57(h) of the Bankruptcy Act[5] (which is not amended

5. See Appendix (*infra*, p. 29).

or affected by Section 77), a creditor has an absolute right to sell collateral, pledged by a bankrupt, in accordance with the contract of pledge.

In *Jerome* v. *McCarter*, 94 U. S. 734 (1876), this Court, considering the rights of a pledgee of the debtor's mortgage bonds, said (p. 739):

> "There is some proof that, when the company became bankrupt (Aug. 28, 1872), some of the bonds were held as collaterals for loans made to the company smaller in amount than the bonds pledged. But the bonds were subsequently sold by the pledgees, and the present holders hold them by absolute right. *The position that the pledgees could not sell the pledge after the adjudication in bankruptcy, is quite untenable. It is sustained by nothing in the Bankrupt Act.*
>
> "* * * Most of those bonds, though at first issued as collaterals for loans *made to the mortgagors*, have been sold, and they are now owned by the purchasers. There are some, it is true, that are still held in pledge; but *the pledgees have a clear right to use them, either by sale or by collection*, until the full amount of the debts due from the mortgagors is satisfied." (Italics ours).

This decision has never been questioned, limited or criticized by any later decision of this Court.

See also *Worth* v. *Marshall Field & Co.*, 240 Fed. 395, 397 (C. C. A. 4th, 1917); *Turner* v. *Metropolitan Trust Co.*, 207 Fed. 495, 499 (C. C. A. 9th, 1913); *In re Ironclad Mfg. Co.*, 192 Fed. 318 (C. C. A. 2nd, 1912); and *Rogers Brown & Co.* v. *Tindel Morris Co.*, 271 Fed. 475, 476 (D. C. E. D. Pa., 1921).

Moreover, the injunctional order here in question was entered in a summary proceeding. (R. 55-58). Clearly in an ordinary bankruptcy proceeding, the court, if it has neither actual nor constructive possession of the property in controversy, cannot adjudicate

a substantial adverse claim thereto in a summary proceeding without the consent of the adverse claimant. *Harrison* v. *Chamberlin,* 271 U. S. 191, 193 (1926); and *Acme Harvester Co.* v. *Beekman Lumber Co.,* 222 U. S. 300, 310 (1911). This Court has apparently recognized that the same rule applies to proceedings under Section 77. See *Ex Parte Baldwin,* 291 U. S. 610, 615 (1934).

Section 77 does not, by its terms, purport to broaden the powers of the district court to enjoin the sale of validly pledged collateral in cases where such sale does not involve *judicial proceedings.* In fact, the statute clearly indicates the contrary.

Subdivision (l) of said Section 77 provides:

> "(l) In addition to the provisions of section 11 of this Act for the staying of pending suits against the debtor, such suits shall be further stayed until after final decree (and)[6] the judge may, upon notice and for cause shown, enjoin or stay the commencement or continuance of any judicial proceeding to enforce any lien upon the estate until after final decree."

Obviously, subdivision (l) was added for the purpose of granting to a bankruptcy court, sitting in railroad reorganization proceedings, the same powers with respect to *pending* suits, involving liens on property in the possession of the debtor, as it has, under the decisions of this Court in *Isaacs* v. *Hobbs Tie & Timber Co.,* 282 U. S. 734 (1931) and *Straton* v. *New,* 283 U. S. 318 (1931), in connection with the enjoining of suits to enforce liens on property in the possession of the bankrupt, commenced *after* the institution of bankruptcy proceedings.

Furthermore, under well settled rules of statutory

6. The word "and" in parentheses was omitted from the statute and is supplied to make sense.

construction, the granting of the power to "enjoin or stay the commencement or continuance of any *judicial proceeding* to enforce any lien upon the estate" impliedly denies power to enjoin the enforcement of liens by sales not involving judicial proceedings. See *In re Heath,* 144 U. S. 92, 93 (1892); *Durousseau* v. *United States,* 6 Cranch 307, 314 (1810); and *Sturges* v. *The Collector,* 12 Wall. 19, 27 (1870).

The pledges involved in this case could under the terms of the collateral notes, and normally would, be enforced through public or stock exchange sales not involving any judicial proceeding.

Subdivision (n) of said Section 77 provides:

> "(n) In proceedings under this section and consistent with the provisions thereof, the jurisdiction and powers of the court, the duties of the debtor and the rights and liabilities of creditors, and of all persons with respect to the debtor and his property, shall be the same as if a voluntary petition for adjudication had been filed and a decree of adjudication had been entered on the day when the debtor's petition was filed."

Certainly in an ordinary voluntary proceeding the court could not have entered the injunction in question, and there is nothing in Section 77 inconsistent with or changing the existing law in this respect.

Subdivision (a) of said Section 77, which provides that the court in a railroad reorganization proceeding, shall

> "during the pendency of the proceedings under this section and for the purposes thereof, have exclusive jurisdiction of the debtor and its property wherever located",

merely obviates the necessity of ancillary bankruptcy proceedings, and does not broaden the power of the bankruptcy court to issue injunctions in cases such as

this case. Section 77 confers no jurisdiction over property not in the possession of the debtor or the bankruptcy court nor over persons not within the district. (See Argument, *ante,* p. 18 and *infra,* p. 24). So far as jurisdiction over property is concerned, Section 77(a) merely restates the pre-existing law practically in the language used by this Court in *Acme Harvester Co.* v. *Beekman Lumber Co.,* 222 U. S. 300, 307 (1911), in *Straton* v. *New,* 283 U. S. 318, 320 (1931), in *Gross* v. *Irving Trust Company,* 289 U. S. 342, 344 (1933) and in *Ex Parte Baldwin,* 291 U. S. 610, 615 (1934).

For example, this Court, in *Acme Harvester Co.* v. *Beekman Lumber Co., supra,* said (p. 307) that it was the purpose of the bankruptcy law

> "to place the property of the bankrupt under the control of the court, wherever it is found * * *."

Nevertheless, this broad jurisdiction over the property of the debtor wherever located did not permit a bankruptcy court to interfere, by injunction, with a pledgee's sale of property where the pledge was valid and the pledged property in the actual possession of the pledgee at the time of the filing of the bankruptcy petition. See *Hiscock* v. *Varick Bank of New York,* 206 U. S. 28, 40 (1907) and *Ex Parte Baldwin,* 291 U. S. 610, 615 (1934).

Although conceding that no express authority for the injunction is conferred by said Section 77, the Circuit Court of Appeals affirmed the order of the District Court on the theory that the power to issue the injunction was conferred as an incident to other powers expressly conferred, saying (R. 324):

> "Our conclusion is that the restraining order is an exercise of authority on the part of the court which was necessary to the effective use of the powers expressly conferred by Congress through this amendment. In short, it was the exercise of

> a power which was incident to those expressly conveyed by Congress to the court."

Sub-clause (15) of Section 2 of the Bankruptcy Act, the "omnibus clause" referred to by the Circuit Court of Appeals (R. 318, footnote*) and apparently relied upon (R. 324), is not new. The present (1898) Act has always included this section which grants general powers to bankruptcy courts to—

> "make such orders, issue such process, and enter such judgments in addition to those specifically provided for as may be necessary for the enforcement of the provisions of this Act; * * *"

This Court, however, referring to said Section 2 (15) in *Ginsberg & Sons* v. *Popkin,* 285 U. S. 204 (1932), said (p. 208):

> "General language of a statutory provision, although broad enough to include it, will not be held to apply to a matter specifically dealt with in another part of the same enactment. * * * Specific terms prevail over the general in the same or another statute which otherwise might be controlling."

The rights of a pledgee, after bankruptcy of the pledgor, are specifically dealt with in other parts of the Bankruptcy Act, for example in Sections 57 (h) and 67(d).[7] Moreover no reason exists why Section 2(15) should confer upon a district court, in a proceeding under Section 77, a power which this Court and other courts have consistently denied to a district court in an ordinary bankruptcy proceeding. There is no such distinction between a bankruptcy *reorganization* proceeding (under Section 77 or Section 77B) and the ordinary bankruptcy *liquidation* proceeding which requires by dubious implication a power in the former proceeding, which the courts have held not to be necessary, or even desirable, in the latter.

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7. See Appendix (*infra*, p. 29).

II.

The District Court Had No Jurisdiction to Issue an Injunction Against the Nonresident Banks.

(*This point is argued only by the nonresident banks*).

It is clear that the District Court would have been without authority to issue an injunction against the nonresident banks upon the facts in this case in an ordinary bankruptcy proceeding. See *Acme Harvester Co.* v. *Beekman Lumber Co.*, 222 U. S. 300, 310 (1911); *Isaacs* v. *Hobbs Tie & Timber Co.*, 282 U. S. 734, 738 (1931); *Progressive Building & Loan Co.* v. *Hall*, 220 Fed. 45 (C. C. A. 4th, 1914).

The court below held, however, that under Section 77 the jurisdictional limits of the District Court are "co-extensive with the territorial boundaries of the United States" and that therefore it could issue a decree *in personam* against the nonresident banks even though they were not within, and held the pledged collateral beyond, the geographical limits of the district.

There is nothing in Section 77, however, which gives to the district court a wider jurisdiction *in personam* than is possessed by a bankruptcy court generally. In fact, the contrary affirmatively appears.

As above pointed out, subdivision (n) of Section 77 provides (p. 20, *ante*):

> "In proceedings under this section and consistent with the provisions thereof, *the jurisdiction and powers of the court * * * shall be the same as if a voluntary petition for adjudication had been filed and a decree of adjudication had been entered on the day when the debtor's petition was filed.*" (Italics ours.)

The statute thus expressly provides that, *unless changed by Section* 77, the jurisdiction and powers of

the court shall be *those possessed by a bankruptcy court in the ordinary bankruptcy proceeding.*

Section 77 contains no provision which expressly or by necessary implication either (a) extends the territorial limits of the district court or (b) extends the power of the court to issue decrees *in personam* against one not within its geographical limits.

The provision upon which the court below based its decision (R. 322) is Section 77 (a), which provides in part (Appendix, *infra*, p. 30):

> "The petition shall be filed with the court in whose *territorial jurisdiction* the railroad corporation * * * has had its principal * * * office, * * *. If the petition is * * * approved, the court * * * shall * * * *have exclusive jurisdiction of the debtor and its property wherever located.*" (Italics ours.)

The particular phrase in question ("exclusive jurisdiction of the debtor and its property wherever located"), which follows a sentence in which the words "territorial jurisdiction" are unmistakably used to refer to the *geographical limits of the judicial district*, does not expressly or by necessary implication make the jurisdictional limits of the district court "co-extensive with the territorial boundaries of the United States."

In terms, the court is given exclusive jurisdiction of (a) "the debtor," and (b) "its property wherever located." This language may be given full effect without "interpreting" it as by *implication* amending the statute fixing the territorial limits of the District Court, or as giving to that court a wider jurisdiction *in personam* with respect to creditors of the debtor than is possessed by a bankruptcy court generally with respect to creditors of the bankrupt.

Convincing proof of the meaning of the phrase "ex-

clusive jurisdiction of the debtor and its property wherever located" is found in decisions of this Court, wherein the Court has repeatedly defined the jurisdiction of a bankruptcy court with respect to the person and property of the bankrupt in language *almost identical to that of the phrase in question. Gross* v. *Irving Trust Co.*, 289 U. S. 342, 344 (1933); *Straton* v. *New*, 283 U. S. 318, 320-321 (1931); *Isaacs* v. *Hobbs Tie & Timber Co.*, 282 U. S. 734, 737 (1931); and *Mueller* v. *Nugent*, 184 U. S. 1, 14 (1902).

Thus, in *Gross* v. *Irving Trust Co., supra*, this Court said (p. 344):

> "Upon adjudication of bankruptcy, title to all the property of the bankrupt, *wherever situated*, vests in the trustee as of the date of filing the petition in bankruptcy. The *bankruptcy court has exclusive jurisdiction, and that court's possession and control of the estate cannot be affected by proceedings in other courts, state or federal.*" (Italics ours)

The use by Congress, in fixing the jurisdiction of the court over the person and property of the debtor in a proceeding under Section 77, of language almost identical with that employed over a long period of years by this Court in describing the jurisdiction of a district court over the person and property of a bankrupt is altogether persuasive evidence that Congress intended that such jurisdictions should be the same. See *The "Abbotsford,"* 98 U. S. 440, 444 (1878).

By statutory provision of long standing, rarely departed from by Congress, "the jurisdiction of a district court *in personam* has been limited to the district of which the defendant is an inhabitant or in which he can be found," and *"It is not lightly to be assumed that Congress intended to depart from a long established policy."* (Italics ours) *Robertson* v. *Railroad*

Labor Board, 268 U. S. 619, 627 (1925); *General Investment Co.* v. *Lake Shore Railway,* 260 U. S. 261 (1922).

The court below placed reliance upon the fact that Section 77 "was intended to * * * exclude ancillary receivership proceedings in bankruptcy cases wherein railroad corporations were the bankrupts." (Rec. 322). But, while Congress intended to eliminate ancillary reorganization proceedings *as such,* with the attendant appointment of ancillary "receivers," it did not declare that the territorial limits of the court should be co-extensive with the United States; nor did it declare that the process of the court might run anywhere in the United States; nor did it give the court such a jurisdiction as necessarily to imply an intent to do either of these things. Just as a bankruptcy court—*though having exclusive jurisdiction of the bankrupt and his property wherever located*—is required to authorize proceedings in a foreign jurisdiction when such step is necessary in order to compel or prevent action by one over whom it has no personal jurisdiction (see cases cited p. 23, *ante*), so the district court under Section 77 is of necessity remitted to similar action in order to accomplish a similar end.

III.

Section 77, as Construed by the Circuit Court of Appeals, Impairs the Contract Rights of Petitioners, Existing at the Date of the Passage of the Act, to Sell the Pledged Collateral, and Therefore Is in Violation of the Fifth Amendment as Applied to Petitioners.

The pledges of collateral security to petitioners were made on August 1, 1932. (R. 38-40, 52-53). Section 77 became effective on March 3, 1933.

This Court has held many times that the Fifth Amendment to the Constitution prohibits the passage by Congress of legislation which operates to impair the obligations of existing contracts. *Lynch* v. *United States,* 292 U. S. 571, 580 (1934); *Hyland* v. *Russell Car & Snow Plow Company,* 279 U. S. 253, 261 (1929); and *Adkins* v. *Children's Hospital,* 261 U. S. 525, 545 (1923).

By far the most important right of a pledgee is the privilege of selling the pledged property at any time after default at which such a sale becomes, in the judgment of the pledgee, advisable. See *In re Hudson River Navigation Corporation,* 57 F. (2d) 175, 176 (C. C. A. 2nd, 1932). The injunctional order in question prohibits a sale of the collateral except at such time or times as the court (*not the pledgee*) may determine that a sale is advisable in the best interests not only of the pledgee, but of the Debtor and its other creditors—and perhaps even of its stockholders. Accordingly a wholly indefinite postponement of a pledgee's right to select the time to realize on the pledged security deprives him not merely of a remedy but of the very essence of the contract. See *Louisiana* v. *City of New Orleans,* 102 U. S. 203, 206 (1880). Section 77, if construed to permit such an injunction, permits the impairment of existing contracts so far as pledgees to whom pledges were made prior to the adoption of said Section 77 are concerned.

The constitutional power of Congress to pass laws "on the subject of bankruptcies" clearly permits legislation which operates to discharge in bankruptcy the *personal* obligation of a debtor to pay his creditors. Congress has, however, no power under the "bankruptcy" clause of the Constitution to pass laws impairing the obligations of existing contracts made by a

bankrupt, if such contracts do not obligate the bankrupt to make any payment to his creditors and merely permit creditors to recover, without the intervention of judicial proceedings, the amount of the debt out of property pledged by the bankrupt. No decision of this Court has ever held that existing rights to enforce liens on or interests in property of the bankrupt, not in the actual or constructive possession of the bankruptcy court, are or may be in any manner impaired by bankruptcy proceedings, so long as such enforcement does not involve judicial proceedings.

Respectfully submitted,

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APPENDIX.

Statutes Involved.

Section 2(15) of the Bankruptcy Act (July 1, 1898, Ch. 541, Sec. 2(15), 30 Stat. 545; U. S. C. A., Title 11, Sec. 11 (15)):

> "The courts of bankruptcy * * * are invested * * * with such jurisdiction at law and in equity as will enable them to exercise original jurisdiction in bankruptcy proceedings. * * * to * * * (15) make such orders, issue such process, and enter such judgments in addition to those specifically provided for as may be necessary for the enforcement of the provisions of this Act."

Section 57(h) of the Bankruptcy Act (July 1, 1898, Ch. 541, Sec. 57(h), 30 Stat. 560; U. S. C. A., Title 11, Sec. 93 (h)):

> "(h) The value of securities held by secured creditors shall be determined by converting the same into money according to the terms of the agreement pursuant to which such securities were delivered to such creditors or by such creditors and the trustee, by agreement, arbitration, compromise, or litigation, as the court may direct, and the amount of such value shall be credited upon such claims, and a dividend shall be paid only on the unpaid balance."

Section 67(d) of the Bankruptcy Act (July 1, 1898, Ch. 541, Sec. 67(d), 30 Stat. 564, as amended by Act of June 25, 1910, Sec. 12, 36 Stat. 842; U. S. C. A. Title 11, Sec. 107(d)):

> "(d) Liens given or accepted in good faith and

not in contemplation of or in fraud upon this Act and for a present consideration * * * shall, to the extent of such consideration only, not be affected by anything herein."

Section 77, sub-clause (a), of the Bankruptcy Act (July 1, 1898, Ch. 541, Sec. 77(a), as added by Act of March 3, 1933, Ch. 204, Sec. 1 (§ 77(a)), 47 Stat. 1474; U. S. C. A., Title 11, Sec. 205(a)):

"(a) Any railroad corporation may file a petition stating that the railroad corporation is insolvent or unable to meet its debts as they mature and that it desires to effect a plan of reorganization. * * * Upon the filing of such a petition, the judge shall enter an order either approving it as properly filed under this section, if satisfied that such petition complies with this section and has been filed in good faith, or dismissing it if not so satisfied. If the petition is so approved, the court in which such order approving the petition is entered shall, during the pendency of the proceedings under this section and for the purposes thereof, have exclusive jurisdiction of the debtor and its property wherever located. * * *"

Section 77(l) of the Bankruptcy Act (July 1, 1898, Ch. 541, Sec. 77(l), as added by Act of March 3, 1933, Ch. 204, Sec. 1 (§ 77(l)), 47 Stat. 1481, U. S. C. A. Title 11, Sec. 205(l)):

"(l) In addition to the provisions of section 11 of this Act for the staying of pending suits against the debtor, such suits shall be further stayed until after final decree (and)[1] the judge may, upon notice and for cause shown, enjoin or stay the com-

1. The word "and" in parentheses was omitted from the statute and is supplied to make sense.

mencement or continuance of any judicial proceeding to enforce any lien upon the estate until after final decree."

Section 77(n) of the Bankruptcy Act (July 1, 1898, Ch. 541, Sec. 77(n), as added by Act of March 3, 1933, Ch. 204, Sec. 1 (§ 77(n)), 47 Stat. 1481; U. S. C. A. Title 11, Sec. 205(n)):

"(n) In proceedings under this section and consistent with the provisions thereof, the jurisdiction and powers of the court, the duties of the debtor and the rights and liabilities of creditors, and of all persons with respect to the debtor and his property, shall be the same as if a voluntary petition for adjudication had been entered on the day when the debtor's petition was filed."

Comparative Statement of the Jurisdictional Provisions of Section 77 and Section 77B of the Bankruptcy Act.

Section 77(a):

"(a) * * * the court in which such order approving the petition is entered shall, during the pendency of the proceedings under this section and for the purposes thereof, have exclusive jurisdiction of the debtor and its property wherever located."

Section 77B(a):

"(a) * * * the court in which such order approving the petition or answer is entered shall, during the pendency of the proceedings under this section, have exclusive jurisdiction of the debtor and its property wherever located for the purposes of this section * * *."

Section 77(c)(1):

"(c) * * * (1) * * * a trustee or trustees * * * who shall have all the title and, subject to the control of the judge and consistently with the provisions of this section, shall exercise all the powers of a trustee appointed pursuant to section 44 or any other section of this Act * * *."

Section 77B(c)(2):

"(c) * * * (2) * * * every such trustee * * * shall have all the title and shall exercise, subject to the control of the judge and consistently with the provisions of this section, all the powers of a trustee appointed pursuant to section 44 of this Act * * *; * * *."

Section 77(l):

"(l) In addition to the provisions of section 11 of this Act for the staying of pending suits against the debtor, such suits shall be further

stayed until after final decree (and)[2] the judge may, upon notice and for cause shown, enjoin or stay the commencement or continuance of any judicial proceeding to enforce any lien upon the estate until after final decree."

Section 77B(c)(10):

"(c) * * * the judge * * * (10) in addition to the provisions of section 11 of this Act for the staying of pending suits against the debtor, may enjoin or stay the commencement or continuation of suits against the debtor until after final decree; and may, upon notice and for cause shown, enjoin or stay the commencement or continuance of any judicial proceeding to enforce any lien upon the estate until after final decree * * *."

Section 77(n):

"(n) In proceedings under this section and consistent with the provisions thereof, the jurisdiction and powers of the court, the duties of the debtor and the rights and liabilities of creditors, and of all persons with respect to the debtor and his property, shall be the same as if a voluntary petition for adjudication had been filed and a decree of adjudication had been entered on the day when the debtor's petition was filed."

Section 77B(o):

"(o) In proceedings under this section and consistent with the provisions thereof, the jurisdiction and powers of the court, the duties of the debtor and the rights and liabilities of creditors, and of all persons with respect to the debtor and its property, shall be the same as if a voluntary petition for adjudication had been filed and a decree of adjudication had been entered on the day when the debtor's petition or answer was approved."

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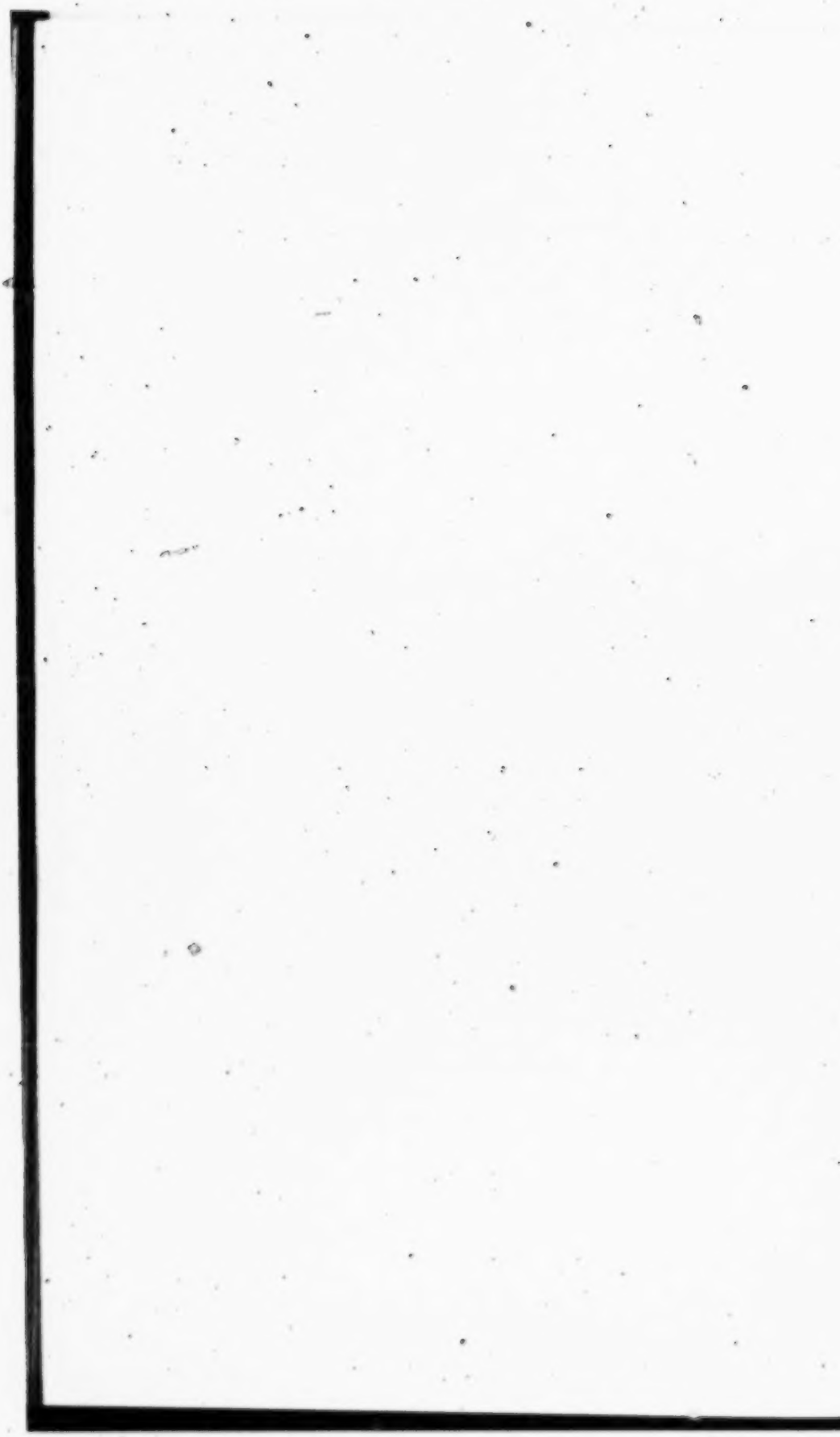
2. The word "and" in parentheses was omitted from the statute and is supplied to make sense.



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CHARLES ELMORE

IN THE

Supreme Court of the United States

OCTOBER TERM, A. D. 1934.

IN THE MATTER

of

THE CHICAGO, ROCK ISLAND & PACIFIC RAILWAY COMPANY, Debtor.

Nos. 479 and 480

CONTINENTAL ILLINOIS NATIONAL BANK AND TRUST COMPANY OF CHICAGO, Petitioner, *vs.* THE CHICAGO, ROCK ISLAND & PACIFIC RAILWAY COMPANY, *et al.*, Respondents.

Nos. 481 and 482

THE CHASE NATIONAL BANK OF THE CITY OF NEW YORK, Petitioner, *vs.* THE CHICAGO, ROCK ISLAND & PACIFIC RAILWAY COMPANY, *et al.*, Respondents.

Nos. 483 and 484

MISSISSIPPI VALLEY TRUST COMPANY, Petitioner, *vs.* THE CHICAGO, ROCK ISLAND & PACIFIC RAILWAY COMPANY, *et al.*, Respondents.

Nos. 485 and 486

HARRIS TRUST AND SAVINGS BANK, Petitioner, *vs.* THE CHICAGO, ROCK ISLAND & PACIFIC RAILWAY COMPANY, *et al.*, Respondents.

Nos. 487 and 488

THE NEW YORK TRUST COMPANY, Petitioner, *vs.* THE CHICAGO, ROCK ISLAND & PACIFIC RAILWAY COMPANY, *et al.*, Respondents.

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

BRIEF FOR PETITIONERS.

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